

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

HONORABLE KATHERINE COOPER

CLERK OF THE COURT
D. Harding
Deputy

JOAN W BRUBACHER

BLAKE E WHITEMAN

v.

PROPAGANDA COMMUNICATIONS INC, et al. LANCE R BROBERG

UNDER ADVISEMENT RULING

On May 11-13, 2015, the parties tried this case to the bench. Having heard and considered the testimony and other evidence and counsels' argument, the Court finds:

1. In favor of Plaintiff Brubacher and against Defendants on Plaintiff's claims for breach of contract, conversion, accounting, and constructive trust; and also on Defendants' claims for breach of contract and breach of fiduciary duty.

2. In favor of Defendants on Plaintiff's claims for breach of fiduciary duty and punitive damages.

3. That Brubacher's membership interest has not yet been redeemed/acquired and, therefore, she is entitled to her buyout and 1/3 share of Resolute distributions paid since September 20, 2013.

4. That the value of Brubacher's interest is \$60,000 pursuant to Section 9.3 of the Operating Agreement and Mr. Probst's calculation.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

5. That Brubacher is entitled to an accounting of Resolute's business activities, income, expenses, and investments.

6. That a constructive trust is imposed over Defendants' assets (exclusive of revenues necessary to pay operating expenses) equal to 1/3 share of Resolute distributions paid since September 20, 2013 plus \$60,000, to be terminated once payment is made.

FINDINGS OF FACT

1. Plaintiff Brubacher filed this action against Resolute Commercial Services, LLC ("Resolute"); Resolute's Members, Propaganda Communications, Inc. ("Propaganda") and JPM, LLC ("JPM"); and the principals of Propaganda and JPM, Jeremiah Foster ("Foster") and John Mitchell ("Mitchell"), respectively, alleging breach of contract, conversion, breach of fiduciary duty, accounting and constructive trust. Defendants asserted counterclaims against Brubacher for declaratory judgment, breach of fiduciary duty, and breach of contract.

2. Brubacher seeks her pro-rata share of Resolute membership distributions from October 1, 2013 until her membership interest is acquired, a buyout of her membership interest, punitive damages, and attorneys' fees.

3. Defendants seek a declaratory order regarding Brubacher's membership in Resolute and the "purchase price" for her membership interest.

4. Defendants did not disclose a computation or evidence of damages in support of their breach of contract and breach of fiduciary duty claims. The Court granted judgment to Plaintiff on those claims at trial.

5. In October, 2009, Brubacher became a Member of Resolute.

6. On June 15, 2011, Brubacher, Propaganda, and JPM entered into an Operating Agreement for Resolute.

7. Under the Operating Agreement, Members each have a one-third membership interest and are entitled to distributions equal to their one-third interest.

8. Section 9.1 of the Operating Agreement provides that if a Member seeks to retire or to withdraw voluntarily from Resolute, the other Members "shall have the right or option to purchase the entire Interest [of the 'Violating Member'] in the Company."

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

9. In June, 2013, Brubacher announced her intention to voluntarily withdraw from Resolute to pursue an opportunity with Beamz.

10. Propaganda and JPM, through Foster and Mitchell, opted to buy her one-third interest.

11. By September 1, 2013, Brubacher left Resolute. There was a transitional period from approximately June 30 through mid-September, 2013, during which she performed limited services on one or two accounts. But she was full-time with Beamz starting September 1, 2013. (Exhs. 38, 40.)

12. On August 1, August 23, and September 20, 2013, Resolute distributed \$10,000, \$20,000, and \$20,000, respectively, to Brubacher. (Exhs. 19, 20, 21.) Resolute also distributed the same amounts on the same dates each to Propaganda and JPM. The parties stipulate that the Members each received another \$10,000 distribution in that same time frame (August-September). Accordingly, the Members received distributions of \$60,000 each on the same dates and in the same amounts. All of the distributions for all three Members are designated "Partner Earnings" in Resolute's records.

13. The \$60,000 described in ¶12 distributed to Brubacher was earnings, not payment for her membership interest.

14. After September 20, 2013, Defendants Propoganda, JPM, Foster, and Mitchell received additional distributions totaling \$1,698,750 for which Brubacher has not received a pro-rata share.

15. Pursuant to Section 8.2 of the Operating Agreement, Brubacher is entitled to receive her one-third distribution after she withdrew until her interest is acquired.

16. Before she left – sometime in July or August, 2013 – Brubacher presented to Foster and Mitchell an outline for calculating the purchase price of her interest. (Exh. 17). The formula consisted of one-third net assets as of June 30, 2013 minus net assets generated before June 30, 2011 (when she joined Resolute), plus one-third share of AZ Tech billings, her laptop, insurance through July 2013, and cell phone through August 2013. The parties discussed a general framework for calculating her buyout. However, there was no binding agreement reached as to the formula for calculating her interest or the value of her interest. There was no agreement or discussion regarding the \$60,000 paid to her in August and September. There was no discussion regarding disbursement of any partner earnings generated by Resolute prior to close on her buyout. Defendants did not accept her proposed preliminary figure of \$169,680 (1/3 partnership interest) plus \$69,680 (anticipated 1/3 share of AZ Tech billings).

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

17. In March, 2014, Brubacher submitted an offer for her interest for \$141,109 to Foster and Mitchell (Exh. 18). This offer did not deduct net assets generated before June 30, 2011, but did include a 1) ten percent withdrawal deduction to net assets, and 2) a credit of \$60,000 (representing the amounts paid to her July-October 2013) against her total one-third share. Foster and Mitchell rejected Brubacher's offer and made a counter that deducted for net assets generated before June 30, 2011, expanded the scope of employee prorated bonuses, and relied on data that differed from Brubacher's figures. (Exh. 16.) Brubacher rejected Defendants' offer and countered with \$124,661. Defendants rejected her \$124,661 and offered \$100,000. Brubacher rejected \$100,000 with no counter. Before sending a demand letter and filing suit, Brubacher submitted a draft Settlement Agreement and Mutual Release to Defendants. They did not accept it.

18. In sum, there were two rounds of negotiations. Brubacher initiated both. The first took place in July-August, 2013 when neither side discussed whether or not she would receive distributions until the other Members acquired her interest and there was no final agreement on the buyout. The second occurred in March, 2014 following her March 20, 2014 email (Exh. 11) in which she stated, "I am entitled to full distributions as a partner until you actually acquire my interest, which has not yet happened."

19. Section 9.1, together with Section 9.3, sets forth the process for determining Brubacher's interest. Section 9.1 expressly provides that, if the remaining Members (Propaganda and JPM) have not exercised their option to buy her interest "within the time limit[s]" prescribed in Section 9.1, she retains the rights of a "Withdrawn Member" as stated in Section 8.2, namely the right to receive distributions until her interest terminates.

20. Pursuant to Sections 9.1 and 9.3, the process for valuing Brubacher's interest is by mutual agreement. If the parties cannot agree, 9.1 provides a metric for calculating the buyout. Alternatively, either party may elect appraisal under Section 9.3. If the parties do not agree on the price as determined by the metric (9.1) and neither side invokes appraisal (9.3), then 9.1 states that Resolute's accounting firm computes the purchase price "which shall be final and conclusive."

21. At all relevant times, Bernard Probst, an independent accountant, acted as Resolute's accountant.

22. After the March, 2014 meeting of the Members, at Mitchell's request, Probst computed the purchase price pursuant to Section 9.1 to be a maximum of \$60,000.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

CONCLUSIONS OF LAW

Breach of Contract

1. Brubacher and Defendants entered into a binding contract, the Operating Agreement. Under Section 8.2, Brubacher is entitled to her 1/3 pro-rata share of membership distributions until her equity interest is acquired. Her interest has not been acquired. The parties negotiated but did not reach an agreement, separate and apart from the Operating Agreement, regarding either the purchase price or the final formula for calculating the purchase price.

2. Defendants breached the Operating Agreement by failing to distribute to Brubacher her 1/3 share of Resolute's distributions from September 20, 2013 (date of last distribution to her) to present.

3. The doctrine of promissory estoppel does not preclude Brubacher's claim for her 1/3 share of Resolute's distributions. Promissory estoppel is reliance on a party's promise to do something in the future. *Trollope v. Koerner*, 106 Ariz. 10, 18, 470 P.2d 91, 99 (1970). There was no evidence that Brubacher promised to decline her Section 8.2 right to her membership interest.

4. The doctrine of equitable estoppel does not preclude her claim for her 1/3 share. To invoke the doctrine, a person must have *reasonably relied* to his detriment on the acts, promises or representations of the adverse party. *Freeman v. Wilson*, 107 Ariz. 271, 485 P.2d 1161 (1971). The evidence fails to support a finding of reasonable reliance by Mitchell and Foster. First, at the time Mitchell and Foster approved the \$1.6 million in distributions to their corporate entities, nothing had been said by either side regarding whether distributions could or would be made to any Member during the negotiation process. Defendants relied on Brubacher's initial proposal made June-July, 2013. In doing so, they relied on a proposal that Defendants did not accept, that they did not finalize with her as receivables were collected, and that did not address future distributions under Section 8.2.

Second, Defendants had the definitive document -- the Operating Agreement -- to consult as to how to proceed in this situation and to determine Brubacher's rights under the Agreement. Mr. Probst, who had no stake in the parties' negotiations, read the Agreement and figured it out. In taking their separate distributions after September 20, it was not reasonable for Defendants to rely on silence, i.e., the absence of any discussion regarding Brubacher's share, over the express language of the Operating Agreement.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

Breach of Fiduciary Duty

5. The Members do not owe each other fiduciary duties. The Operating Agreement governs the relations among the members and does not include fiduciary duties. A.R.S. § 29-682(B) (“An operating agreement governs relations among the members and the managers and may contain any provision that is not contrary to law and that relates to duties or powers of its members”); *TM2008 Investments, Inc. v. Procon Capital Corp.* 234 Ariz. 421, 424. 323 P.3d 704, 707 (2014).

6. The Court does not reach the issue of whether Foster and Mitchell became “controlling members,” thereby assuming a fiduciary duty to Brubacher because, even if they did, the evidence does not support a finding of breach. Foster and Mitchell negotiated with Brubacher. They reserved funds (\$100,000) for the purchase price. They allowed her access to Resolute’s books and records after she left. While they erred in taking distributions without settling up with Brubacher, the Court does not find that they engaged in gross negligence, reckless conduct, intentional misconduct, or a violation of the law.

Action for Accounting

7. Brubacher is entitled to her 1/3 membership draws until her interest is acquired pursuant to Sections 6.1 and 8.2 of the Operating Agreement and A.R.S. §29-707.

8. Resolute violated Section 29-707 by making distributions to Propaganda and JPM, but not Brubacher, since September 20, 2013 totaling approximately \$1,698,750.

9. Propaganda and JPM violated Sections 6.1 and 8.2 of the Operating Agreement by failing to distribute to Brubacher her 1/3 share of \$1,698,750.

10. Defendants are required to provide Brubacher with a full, complete, and accurate accounting in accordance with GAAP standards of all business activities, income, expenses, and investments.

Conversion

11. Propaganda and JPM are liable for conversion. They knowingly and intentionally took \$1,698,750 in Resolute distributions. Brubacher has a possessory interest in a 1/3 pro rata share of those distributions. By making the \$1,698,750 distributions to themselves, Propaganda and JPM exercised dominion and control over Brubacher’s 1/3 share (\$566,250) and interfered with her Section 8.2 right to her share. As a result of Propaganda and JPM’s conduct, Brubacher incurred damages.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

12. Mitchell (as Manager of JPM) and Foster (as President of Propanda) are also liable for conversion. They authorized Resolute to make the distributions to Propaganda and JPM, but not to Brubacher, after September 20, 2013. As a result, they participated in converting funds that belonged to Brubacher. They were also negligent in managing Resolute's corporate affairs by allowing Resolute to make distributions to Propaganda and JPM without first finalizing an agreement with Brubacher and/or disbursing to her one-third share. Their negligence caused or contributed to a conversion of the distributions owed to Brubacher under the Operating Agreement. *Jabczenski v. Southern Pacific Memorial Hospitals*, 119 Ariz. 15, 20, 579 P.2d 53, 58 (1978).

Punitive Damages

13. To recover punitive damages, Brubacher had to show, by clear and convincing evidence, that Defendants acted with an evil mind, that is, that they intended to injure her or consciously pursued a course of conduct knowing that it created a substantial risk of significant harm. *Rawlings v. Apodaca*, 151 Ariz. 149, 726 P.2d 565 (1986); *Gurule v. Illinois Mutual Life & Casualty Co.*, 152 Ariz. 600, 734 P.2d 85 (1987).

14. Based on the evidence, the Court does not find that Defendants acted with the requisite evil mind.

RULING

IT IS HEREBY ORDERED:

1. Defendants are liable to Brubacher on her claims for breach of contract, conversion, accounting and constructive trust; and also on Defendants' claims for breach of contract and breach of fiduciary duty.

2. Defendants are not liable on Plaintiff's claims for breach of fiduciary duty and punitive damages.

3. Brubacher is awarded her damages of \$60,000 (membership interest) plus her pro-rata share of distributions made by Resolute between September 20, 2013 (date of last distribution to her as shown by the evidence) and the date of payment of the membership interest, a minimum of \$566,250 (1/3 of \$1,698,750) plus interest at the legal rate from the date that a Judgment is entered until paid.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2014-008042

05/15/2015

4. Brubacher is entitled to an accounting of Resolute's business activities, income, expenses, and investments. The accounting shall be completed and provided to Plaintiff no later than **June 22, 2015**.

5. Effective the date of this Order, a constructive trust is imposed over Defendants' assets (exclusive of revenues necessary to pay operating expenses) equal to \$60,000 plus 1/3 share of Resolute distributions owed to Brubacher pursuant to the Operating Agreement and this Order, to be terminated once payment is made.

6. Brubacher is entitled to recover her reasonable attorneys' fees and costs pursuant to A.R.S. §12-341.01. Brubacher shall submit an Application by **July 30, 2015**.